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ACTION ARA-10

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FM AMEMBASSY ASUNCION

TO SECSTATE WASHDC 6459

INFO AMEMBASSY BRASILIA 0626

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C O N F I D E N T I A L ASUNCION 0079

E.M. 11652: GDS

TAGS: EGEN, EAID, PA

SUBJ: CEPICIES PARAGUAY COUNTRY REVIEW

REF: STATE 75 304866

SUMMARY. EMBASSY CONSIDERS THAT LOCAL PRESS REPORTS AND COMMENTS CONTAINED REFTEL COVERING RECENT CEPICIES PARAGUAY COUNTRY REVIEW IN WHICH THE PRESENT STATE OF THE ECONOMY WAS CATEGORIZED AS "POSITIVE", "DYNAMIC" AND "ENCOURAGING" ARE MISLEADING AND CANNOT BE JUSTIFIED BY DATA PRESENTLY AVAILABLE. CHIEFLY BECAUSE OF INCREASED COST OF OIL IMPORTS AND A SIGNIFICANT DROP IN MEAT EXPORTS, PARAGUAY EXPERIENCED A SERIOUS BALANCE OF TRADE DEFICIT DURING THE PAST TWO YEARN WHICH IS EXPECTED TO CONTINUE IN 1976. THE BUILD-UP IN FOREIGN EXCHANGE RESERVES OCCURRED DESPITE THIS DEFICIT BECAUSE OF SIZEABLE SHORT-TERM CREDITS FROM BRAZIL AND ARGENTINA AND SEVERAL LARGE LOANS FROM INTERNATIONAL LENDING

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INSTITUTIONS. ANY HOPED-FOR IMPACT ON THE ECONOMY

FROM THE LARGE HYDROELECTRIC PROJECT AT ITAIBE WILL NOT OCCUR FOR MORE THAN A DECADE BOTH BECAUSE THE SYSTEM WILL BEGIN FULL OPERATION ONLY IN MID-1980'S AND BECAUSE THE GOP HAS MORTGAGED TO BRAIL ITS SHARE OF FUTURE REVENUES FROM THE PROJECT FOR MANY YEARS BEYOND THAT POINT. END SUMMARY.

1. LOCAL PRESS ACCOUNTS OF THE CEPICIES' COUNTRY REVIEW FOR PARAGUAY WHICH WAS HELD IN WASHINGTON FROM DECEMBER 15 THROUGH 18 HAVE UNIFORMLY EMPHASIZED EXPRESSIONS OF APPROVAL REPORTEDLY

RECEIVED FROM PARTICIPATING AGENCIES OVER THE "VERY POSITIVE" PRESENT CONDITION OF THE PARAGUAYAN ECONOMY. IT IS NOT CLEAR, FROM COMPARING REFTEL WITH PRESS ACCOUNTS, WHAT PERIOD OF PERFORMANCE WAS REVIEWED. PRESS STORIES REFER TO 1973 AND 1974, WHILE REFTEL MENTIONS "LAST YEAR". FOR EXAMPLE, PRESS ACCOUNTS UNDERSCORE THE INCREASE IMPORTS WHICH AMOUNTED TO 33.8 PERCENT FROM 1973 TO 1974 DESCRIBING THIS AS "NOTEWORTHY DYNAMISM IN NON-TRADITIONAL AGRICULTURAL EXPORTS." ACCORDING TO THESE PRESS ACCOUNTS THIS JUMP IN EXPORTS ENABLED PARAGUAY TO INCREASE ITS FOREIGN EXCHANGE RESERVES FROM 38.5 MILLION DOLLARS IN 1972 TO 83 MILLION DOLLARS IN 1975.

2. THE EMBASSY IS CONCERNED SINCE THE GLOWING PICTURE OF THE PRESENT STATE OF PARAGUAY'S ECONOMY REPORTEDLY PRESENTED AT THE CEPICIES MEETING IS MISLEADING AND CANNOT BE JUSTIFIED. DURING THE PERIOD DESCRIBED IN THE NEWSPAPER ACCOUNTS (1973-75), PARAGUAY'S TRADE DEFICIT INCREASED FROM A SMALL POSITIVE BALANCE IN 1973 TO A 28.5 MILLION DOLLAR DEFICIT IN 1974 AND THIS YEAR WILL EXCEED 35 MILLION DOLLARS. THIS SITUATION DEVELOPED DESPITE UNUSUALLY HIGH WORLD MARKET PRICES FOR SEVERAL AGRICULTURAL COMMODITIES WHICH PARAGUAY EXPORTS, AND WAS DUE PRINCIPALLY TO THE GREATLY INCREASED COST OF

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PETROLEUM IMPORTS AND A SERIOUS DROP IN MEAT EXPORTS (TRADITIONALLY PARAGUAY'S LEADING EXPORT). THIS SHARP INCREASE IN TRADE DEFICIT WOULD HAVE CAUSED A SERIOUS BALANCE OF PAYMENTS DEFICIT IF IT HAD NOT BEEN FOR THE CONTINUED FLOW OF BOTH SHORT AND LONG TERM FOREIGN CREDITS. THE INCREASE IN FOREIGN EXCHANGE RESERVES IS ALMOST EXCLUSIVELY BASED ON SUPPLIER CREDIT PROVIDED BY BRAZIL AND ARGENTINA

FOR THE PURCHASE OF PRODUCTS MANUFACTURED IN THOSE TWO COUNTRIES PLUS THE MORE SIZEABLE LOANS GRANTED BY INTERNATIONAL LENDING INSTITUTIONS.

3. IN THE EMBASSY'S VIEW PROSPECTS FOR 1976 REMAIN LITTLE CHANGED FROM THOSE EXPERIENCED IN 1975, I.E., A CONTINUED TRADE DEFICIT, WITH THE PROBABILITY THAT FOREIGN EXCHANGE RESERVES WILL BE DRAWN DOWN SOMEWHAT.

4. AS DISCUSSED IN REFTTEL, THE COMPLETION OF THE HYDROELECTRIC PROJECT AT ITAIPU UNQUESTIONABLY WILL HAVE A PROFOUND EFFECT ON PARAGUAY. HOWEVER, IF PARAGUAY CONTINUES AT THE PRESENT RATE TO MORTGAGE ANTICIPATED FUTURE REVENUES FROM ENERGY EXPORTS, IT MAY BE SEVERAL DECADES BEFORE ANY ECONOMIC ADVANTAGE IS DERIVED FROM THE HYDROELECTRIC SYSTEM. THE ITAIPU PROJECT WILL NOT BE COMPLETED UNTIL 1984 AT EARLIEST, AND

IT MAY BE SEVERAL YEARS BEYOND THAT BEFORE THE FULL SYSTEM IS IN OPERATION. THEORETICALLY HALF OF THE POWER GENERATED WILL BELONG TO PARAGUAY AND CAN BE USED DOMESTICALLY OR SOLD TO BRAZIL. IT IS PRESUMED LOCALLY THAT IT WILL BE SOLD. THROUGH A SERIES OF LOANS FOR THE CAPITALIZATION OF THE ITAIPU BINATIONAL ENTITY AND THE LOCAL COSTING OF THE CONSTRUCTION (NOT INCLUDING THE GENERATING AND POWERHOUSE EQUIPMENT) PARAGUAY HAS EFFECTIVELY MORTGAGED TO BRAZIL THE FUTURE REVENUES FROM THE PROJECT FOR MANY YEARS. PARAGUAY WILL PROBABLY NOT CHANGE FROM A NET IMPORTER TO A NET EXPORTER OF ENERGY WITHIN THE TIME FRAME OF

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INTEREST TO PRESENT DAY ANALYSTS.

5. AS NOTED IN REFTTEL, THERE REMAINS MUCH TO BE DONE WITHIN THE GOP TOWARD PUTTING FISCAL AND PUBLIC INVESTMENT REFORMS INTO EFFECT. EMBASSY AGREES THAT ANY MEANINGFUL ACHIEVEMENT IN THIS DIRECTION WOULD MEAN A MAJOR DEPARTURE FROM PARAGUAY'S PAST PERFORMANCE.

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